

Message Text

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ACTION AID-59

INFO OCT-01 ADP-00 EA-04 EB-05 IGA-02 INR-10 SS-07 /088 W
----- 008011

R 210350 Z APR 73
FM AMEMBASSY JAKARTA
TO SECSTATE WASHDC 6548

C O N F I D E N T I A L SECTION 1 OF 2 JAKARTA 4674

E. O. 11652: XGDS

SUBJ: MAY 1973 IGGI MEETING

AIDAC

REF: A) STATE 067975 (CL)
B) JAKARTA 4165 (CL)
C) JAKARTA 4538 (UC)
D) JAKARTA 4392

1. SUMMARY. ALTHOUGH IBRD AND IMF DELEGATIONS OR GOI ITSELF LIKELY INITIATE DISCUSSION MOST OF FOLLOWING ISSUES, USG DELEGATION SHOULD BE PREPARED DISCUSS OR RAISE FOLLOWING ITEMS AS APPROPRIATE. END SUMMARY.

2. RICE. REFTEL B REVIEWS CURRENT RICE OUTLOOK IN CONTEXT PL 480 ASSISTANCE. IN REGARD LONG- TERM, WE CONCUR IN GENERAL WITH IBRD ASSESSMENT (P 35-37, VOLUME III, THE AGRICULTURE SECTOR, IBRD REPORT 25- IND). HOWEVER, OUR OPINION IS THAT PROGRESSIVELY FALLING REAL RICE PRICES DESIRABLE IN INDONESIA CONTEXT ONLY AFTER UPWARD TREND IN PRODUCTION CLEARLY ESTABLISHED. WE FULLY SUPPORT IBRD CONCLUSION THAT CURRENT HIGH DELIVERY COST OF GETTING RICE PRODUCED ON OUTER ISLANDS TO JAVA MARKETS IS A KEY BOTTLENECK TO INCREASED INDONESIAN RICE PRODUCTION.

3. MEDIUM- TERM BORROWING. WASHINGTON FULLY INFORMED DEVELOPMENTS THIS AREA. WE ASSUME GOI AND IMF WILL DISCUSS SUBJECT AT IGGI. PRESUMABLY DISCUSSION WILL INCLUDE ASSESSMENT IMPACT PAST BORROWINGS ON DEBT PROFILE AS WELL AS REVIEW OF EVALUATION
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AND CONTROL PROCEDURES ESTABLISHED DEAL WITH FUTURE BORROWINGS. GIVEN MAGNITUDES INVOLVED (COMPARABLE TO IGGI ASSISTANCE),

BELIEVE IT DESIRABLE AND TIMELY TO DISCUSS RELATIONSHIPS BETWEEN MAGNITUDES, COMPOSITION AND ROLES ASSISTANCE WITHIN IGGI FRAMEWORK AND FOREIGN FINANCING OUTSIDE IGGI TO PUBLIC ENTERPRISES.

4. SUBSIDIES. IN KEEPING WITH DECEMBER IGGI GOI STATEMENT THAT WHEAT AND COTTON SUBSIDIES WOULD BE REDUCED, WE UNDERSTAND EXCHANGE RATE FOR COTTON IMPORTS TO BE INCREASED FROM RP 271/ US \$ TO RP 320/ US \$. TO ENCOURAGE REALIZATION THIS PLANNED INCREASE, BELIEVE GOI SHOULD BE ASKED TO REPORT ON STATUS COTTON SUBSIDY PROGRAM. MEANWHILE WHEAT PRICING SITUATION HAS GOTTEN SIGNIFICANTLY WORSE SINCE DECEMBER. ALTHOUGH GOI RECENTLY INCREASED C AND F PRICE WHEAT GRAIN CHARGED MILLERS FROM RP 21.75/ KG TO RP 27.50/ KG, WORLD MARKET PRICE WHEAT GRAIN LANDED JAKARTA IS NOW ABOUT RP 50/ KG. EFFECT HAS BEEN INCREASE OF PREVIOUS RP 9/ KG SUBSIDY ON GRAIN PURCHASES TO RP 22.5/ KG. THIS MIGHT BE ACCEPTABLE SITUATION IF INTENT AND EFFECT OF GOI POLICY WAS TO ASSURE INEXPENSIVE WHEAT PRODUCTS FOR CONSUMERS AND IF CONSUMERS WERE RELATIVELY POOR FRACTION OF SOCIETY. FACT IS HOWEVER, CONSUMERS WHEAT PRODUCTS TEND NOT TO BE RELATIVELY POOR

AND GOI POLICY CLEARLY DESIGNED PERMIT MILLERS AND WHOLESALE SYNDICATE OBTAIN EXCESS PROFITS FROM HIGH PRICES THAT RESULT THEIR AUTHORIZED MONOPOLY POSITION. THESE PROFITS ARE AT EXPENSE GOI COUNTERVALUE REVENUES. AT PRESENT TIME MILLERS SELL FLOUR BETWEEN RP 62.2 AND 64.63 / KG, DEPENDING ON QUALITY, (A RP 16/ KG INCREASE WAS AUTHORIZED AT SAME TIME GRAIN PRICE INCREASED TO RP 27.5) AND BY PRODUCTS AT RP 20/ KG. OPERATING COSTS ESTIMATED AT 6-7 RP/ KG. MILLERS ALSO PAY ABOUT RP 5/ KG WHEAT FLOUR IN OFFICIAL LEVIES AND TAXES. (WORTH NOTING RP 2 OF THIS GOES TO GOVERNMENT SLUSH FUND OUTSIDE BUDGETARY CONTROL). MILLING PROFITS APPEAR TO BE ABOUT RP 20/ KG FLOUR SOLD. FLOUR DISTRIBUTION SYNDICATE PURCHASES FLOUR EX MILL AT RP 62.5/ KG. CURRENT RETAIL PRICE RP 85-90/ KG. COST OF DISTRIBUTION ALMOST CERTAINLY LESS THAN RP 10 / KG. DISTRIBUTION PROFITS THEREFORE ABOUT RP 15/ KG. MILLING AND DISTRIBUTION PROFITS TOTAL ABOUT RP 35/ KG FLOUR SOLD. AT CURRENT RATE WHEAT CONSUMPTION, THIS EQUIVALENT APPROXIMATELY \$35 MILLION PER YEAR. IT SEEMS CLEAR THAT EXCESS PROFITS ARE AT EXPENSE OF GOI COUNTERVALUE RECEIPTS. PREFERABLE PRICE POLICY WOULD BE FOR GOI TO CHARGE MILLERS AT LEAST WORLD MARKET PRICE FOR WHEAT GRAIN. INDEED, GIVEN MONOPOLY

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POSITION OF MILLERS, GOI SHOULD BE PREPARED ADJUST THIS PRICE UPWARD IF RETAIL PRICES INDICATE EXCESS PROFITS BEING RECEIVED. FYI WE UNDERSTAND RELATIVES OF PRESIDENT ARE CLOSELY ASSOCIATED WITH TWO OF THREE FLOUR MILLS IN INDONESIA AND THAT GOVERNMENT PRICE POLICY IN THIS AREA IS NOT DETERMINED OR NECESSARILY APPROVED BY ECONOMIC MINISTRIES. END FYI. WITH REGARD RICE SUBSIDIES, WE DO NOT BELIEVE THERE IS A PROBLEM CURRENTLY. INDONESIAN DOMESTIC PRICES AND GOI PRICING POLICY APPEAR APPROPRIATELY DESIGNED IN TERMS WORLD MARKET PRICES,

COUNTERVALUE RECEIPTS AND PRODUCTION INCENTIVES.

5. UNTYING. WE BELIEVE U. S. POSITION TAKEN LAST DECEMBER APPROPRIATE. IT WOULD BE USEFUL IF JAPANESE WOULD CLARIFY WHAT THEIR UNTYING PRACTICES ARE VIS- A- VIS INDONESIA.

6. EDUCATION. WE WOULD WELCOME GOI STATEMENT CONCERNING STATUS THEIR PLANS EDUCATION SECOTR AND WHAT ROLE THEY ENVISION FOR IGGI. BELIEVE IT ALSO VERY USEFUL TO HAVE GOI COMMENTS ON NATIONAL ASSESSMENT OF EDUCATION, WHEN VARIOUS PORTIONS WILL BE FINISHED, AND WHEN REPORTS MIGHT BE MADE AVAILABLE INTERESTED DONORS.

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INFO OCT-01 ADP-00 EA-04 EB-05 IGA-02 INR-10 SS-07 /088 W

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R 210350 Z APR 73

FM AMEMBASSY JAKARTA

TO SECSTATE WASHDC 6549

C O N F I D E N T I A L SECTION 2 OF 2 JAKARTA 4674

AIDAC

SUBJ: MAY 1973 IGGI MEETING

7. PRIVATE INVESTMENT. GOI HAD PLANNED ANNOUNCING LAST JANUARY REVISED AND SIMPLIFIED PROCEDURES APPLICABLE FOREIGN AND DOMESTIC PRIVATE INVESTMENT. DUE TO CONCENTRATION KEY OFFICIALS ON INTERNAL RICE SITUATION THIS WAS DELAYED AND WE UNDERSTAND RECOMMENDATIONS HAVE NOT YET GONE FORWARD TO PRESIDENT (REF D). WOULD BE USEFUL IF GOI DELEGATION REVIEWED CURRENT STATUS AND ASKED TO INDICATE WHEN NEW PROCEDURES WILL BE FINALIZED AND IMPLEMENTED.

8. INTEREST RATE REFORM. GOI RECENTLY DECREASED SPREAD OF INTEREST RATES APPLICABLE DOMESTIC BORROWING BY LOWERING HIGHER INTEREST RATES (SEE REFTEL C). MAJORITY OF LENDING RATES NOW LIE BETWEEN 12 AND 18 PER CENT PER ANNUM. RATES PAYABLE ON TIME DEPOSITS ALSO REDUCED. WE UNDERSTAND PRIMARY REASONS REVISION ARE : (1) TO DECREASE INFLOW OF POTENTIALLY VOLATILE FOREIGN TIME DEPOSITS, (2) TO REDUCE RATE ACCELERATION OF INCREASES IN DOMESTIC TIME DEPOSITS TO PROVIDE STATE BANKS TIME TO IMPROVE THEIR OPERATIONS, (3) TO REDUCE SPREAD BETWEEN BORROWING AND LENDING INTEREST RATES FOR STATE BANKS SO AS TO FORCE MORE EFFICIENT OPERATION, (4) TO REDUCE COST OF CREDIT FOR OPERATING CAPITAL AND EXPORT ACITIVITIES,(5) TO REDUCE THE INCENTIVES FOR MISREPRESENTING THE PURPOSES FOR WHICH LOANS INTENDED SO AS TO OBTAIN CREDIT AT

THE LOWEST RATE, AND (6) TO INCREASE FRACTION AVAILABLE CREDIT GOING TO SMALLER INVESTORS. ALTHOUGH WE HAVE NO REAL DISAGREEMENT VALIDITY ABOVE OBJECTIONS, WE ARE CONCERNED THAT DECREASE IN INTEREST RATES AND PARTICULARLY CONTINUATION INFLEXIBLE AND ARTIFICIAL RATE STRUCTURE MAY NOT BE BEST WAY OF ACHIEVING THEM. BASED ON PERFORMANCE PRIOR RICE SHORTAGE INFLATION WAS RUNNING ROUGHLY 8-10 PERCENT AND MARKET RATE OF INTEREST WAS PROBABLY
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ABOUT 20 PERCENT. WE BELIEVE CONTINUATION SUBSIDIZED LENDING RATES, E. G. 12 PERCENT IS UNDESIRABLE. FYI WE UNDERSTAND THAT CONSIDERABLE PRESSURE WAS PLACED ON THE ECONOMIC MINISTRIES TO LOWER THE 12 PERCENT LENDING RATE FOR MEDIUM TERM CREDITS. THAT THIS WAS SUCCESSFULLY RESISTED IS FORTUNATE. END FYI. WE BELIEVE THAT COMMENTS BY THE GOI AT IGGI CONCERNING THEIR POLICIES IN THIS AREA WOULD BE USEFUL. A DISCUSSION OF THE ROLE OF THE STATEBANKS AND ANY PROBLEM AREAS IN THEIR OPERATIONS WOULD ALSO BE DESIRABLE.

9. PROJECT COUNTERPART BUDGET. MOST PROJECTS FINANCED BY IGGI BETWEEN 1967-71 ARE JUST NOW BEGINNING TO MOVE INTO CONSTRUCTION PHASE WHICH REQUIRES INCREASING DISBURSEMENT GOI LOCAL CURRENCY COMMITTED AS PART OF FINANCING AGREEMENTS. (UNDISBURSED BALANCE OF FOREIGN PROJECT LOANS AS OF 12/31/72 IN EXCESS US \$900 MILLION). GOI HAS PREVIOUSLY TAKEN POSITION THERE HAS BEEN NO FAILURE SHOWN OF GOI BUDGET SUPPORT FOR THESE PROJECTS AND OUR KNOWLEDGE THIS IS CORRECT. WITHOUT WISHING BELABOR ISSUE, IT MIGHT BE USEFUL TO RAISE FUTURE BUDGETARY IMPLICATIONS OF CURRENT PROGRAMS WITH THE GOI IN THE IGGI FORUM. A STATEMENT OR CLARIFICATION BY THE GOI OF ITS PLANNING OF BUDGET SUPPORT FOR THESE AND FUTURE PROJECTS WOULD BE HELPFUL.

10. EMPLOYMENT/ EQUITY/ REGIONAL DEVELOPMENT. WE WOULD WELCOME GOI DELEGATION REVIEW CURRENT STATUS FORMULATION THEIR POLICIES AND PROGRAMS THESE AREAS. WE UNDERSTAND GOI SEEKING TO HAVE REGIONAL DEVELOPMENT PLANS PREPARED BY IGGI DONORS FOR SEVERAL AREAS INDONESIA. BELIEVE WOULD BE DESIRABLE FOR GOI DISCUSS THEIR VIEW PROPER BALANCE BETWEEN REGIONAL DEVELOPMENT, CENTRALIZED DECISION- MAKING IN JAKARTA, AND ALLOCATION DEVELOPMENT RESOURCES DURING COURSE NEXT FIVE YEAR PLAN. IN CONTEXT RURAL DEVELOPMENT AND EMPLOYMENT CREATION, GOI HAS SUPPORTED STEADY EXPANSION KABUPATEN PUBLIC WORKS AND VILLAGE SUBSIDY PROGRAMS. THESE PROGRAMS RELATIVELY SMALL FRACTION TOTAL DEVELOPMENT EFFORT (ABOUT 7 PERCENT). WE AGREE WITH IBRD CONCLUSION (PAGE 22, VOLUME V, EMPLOYMENT PERSPECTIVES, IBRD REPORT 25- IND) THAT SIGNIFICANTLY GREATER EFFORT MAY BE REQUIRED TO COPE WITH UNEMPLOYMENT PROBLEM ON JAVA AND MADURA. WOULD WELCOME GOI COMMENTS THIS AREA. TOUSSAINT

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Message Attributes

Automatic Decaptioning: X
Capture Date: 07 MAY 1999
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: n/a
Control Number: n/a
Copy: SINGLE
Draft Date: 21 APR 1973
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: golinofr
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1973JAKART04674
Document Source: ADS
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: n/a
Film Number: n/a
From: JAKARTA
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1973/newtext/t19730460/abqcefei.tel
Line Count: 217
Locator: TEXT ON-LINE
Office: ACTION AID
Original Classification: CONFIDENTIAL
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 4
Previous Channel Indicators:
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: n/a
Reference: A) STATE 067975 (CL) B) JAKARTA 4165 (CL) C) JAKARTA 4538 (UC) D) JAKARTA 4392
Review Action: RELEASED, APPROVED
Review Authority: golinofr
Review Comment: n/a
Review Content Flags:
Review Date: 21 NOV 2001
Review Event:
Review Exemptions: n/a
Review History: RELEASED <21-Nov-2001 by martinml>; APPROVED <22 FEB 2002 by golinofr>
Review Markings:

Declassified/Released
US Department of State
EO Systematic Review
30 JUN 2005

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: <DBA CORRECTED> jms 980127
Subject: MAY 1973 IGGI MEETING
TAGS: EFIN, n/a
To: STATE
Type: TE
Markings: Declassified/Released US Department of State EO Systematic Review 30 JUN 2005